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LEGISLATIVE ISSUES IN PROPOSALS AFFECTING THE
TAX TREATMENT OF COMMODITIES
RECEIVED UNDER THE PAYMENT-IN-KIND (PIK) PROGRAM

Joint Committee on Taxation
February 23, 1983
JCX-4-83

ISSUE	PRESENT LAW	PROPOSED ALTERNATIVE
1. Timing of Income	For cash basis taxpayers, income is recognized when actually or constructively received. Accrual method taxpayers recognize income when all events have occurred that fix the right to receive the income and the amount can be reasonably estimated. Under present law, PIK payments will be recognized as income on the date they are made available to farmers.	Recognition of income from PIK payments in a 1983 PIK program would be deferred from the date the commodities are received (or constructively received) to the date they are sold by the farmer. An anti-speculation rule would limit the deferral of income provisions to property owned on February 23, 1983, or to property inherited or acquired by gift from an individual who owned it on February 23, 1983.
2. Current Use Valuation for Estate Tax Purposes	Real property to be specially valued must be used in an active farming use for 5 years of the 8-year period before a decedent's death and on the date of death. Qualified heirs must use specially valued property in an active farming use throughout a prescribed period to avoid imposition of a recapture tax. An individual is treated as using property in farming only if the individual is at risk as to price and production.	Real property withdrawn from production in exchange for a payment-in-kind under the 1983 PIK program would be treated as used in an active farming operation in which the person entering the PIK contract was at risk.

J862-40

ISSUE

PRESENT LAW

PROPOSED ALTERNATIVE

Only property with respect to which material participation requirements are satisfied is eligible for current use valuation. These requirements apply to both the pre-death and recapture period.

An individual who materially participates in the conservation use to which property withdrawn from production under the PIK program is put is considered to satisfy the current use valuation material participation requirement.

An anti-speculation rule would limit the estate tax provisions to property owned on February 23, 1983, or to property inherited or acquired by gift from an individual who owned it on February 23, 1983.

Effective date.--These provisions would apply to land withdrawn from production during the 1983 crop year pursuant to the 1983 PIK program.

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3. Payments of Estimated Tax	Persons whose estimated gross income from farming is at least two-thirds of their total estimated gross income are not required to pay quarterly installments of estimated tax if their returns are filed and tax is paid in full by March 1. No underpayment penalty will be imposed if estimated tax payments are at least 66-2/3 percent of the tax for the year.	Commodities received under a 1983 PIK program would be treated as gross income from farming.
4. Method of Accounting by Corporations Engaged in Farming	Farming corporations, other than certain "family-owned" and other small corporations must use accrual accounting. These small corporations may use the cash method.	Commodities received under a 1983 PIK program would be treated as income from farming.
5. Soil and Water Conservation Expenditures	Taxpayers engaged in the trade or business of farming can elect to expense certain amounts which are paid or incurred for the purpose of soil or water conservation with respect to land used for farming.	Property withdrawn from production under a 1983 PIK program would be treated as used by the taxpayer in the trade or business of farming; commodities received under a 1983 PIK program would be treated as income from farming.

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6. Expenditures by Farmers for Fertilizer, etc.	Taxpayers engaged in the trade or business of farming may elect to expense amounts otherwise chargeable to capital account which are paid to enrich, neutralize, or condition land used in farming.	Property withdrawn from production under a 1983 PIK program would be treated as used by the taxpayer in the trade or business of farming.
7. Expenditures by Farmers for Clearing Land	Taxpayers engaged in farming may elect to deduct currently expenditures, subject to certain limitations, for clearing land.	A taxpayer receiving commodities under a 1983 PIK program would be treated as engaged in the business of farming with respect to land withdrawn from production under the 1983 PIK program.
8. Activities not Engaged in for Profit	If an individual or subchapter S corporation engages in an activity not for profit, generally no deductions in excess of the income attributable to such activity are allowed.	A taxpayer receiving commodities under a 1983 PIK program would not be treated as not engaged in an activity for profit solely by reason of participation in the PIK program.
9. Gain from Disposition of Property Used in Farming or Farm Losses Offsetting Farm Income	Taxpayers are prevented from taking ordinary loss deductions attributable to farming with respect to pre-1976 taxable years and then selling the farm property at capital gain rates.	Commodities received under a 1983 PIK program would be treated as gross income from farming.

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10. Qualification of Corporations for Subchapter S Status	For corporations which had accumulated earnings and profits before electing subchapter S status, passive income within the 3 taxable years before such election cannot exceed 25 percent of gross receipts.	Commodities received under a 1983 PIK program would not be treated as passive income in determining a corporation's eligibility for subchapter S status.
11. Self-Employment Income	Earned income is subject to self-employment income (SECA) tax. An individual's farm income is "earned" for SECA purposes if the individual materially participates in the farm operation. Present law provides for reduction of social security benefits payable to individuals below age 70 if the individual's earned income exceeds a prescribed amount.	Commodities received under a 1983 PIK program would be treated as earned income for SECA tax purposes. Commodities received under a 1983 PIK program would be treated as earned income for social security benefit purposes.

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12. Tax Treatment of Payments-In-Kind Marketed Through Co-operatives	Cooperatives (both exempt and non-exempt) are allowed to exclude from income amounts paid to members or patrons as patronage dividends or per-unit retain allocations, where such amounts are earned from marketing commodities produced by members or patrons. Such payments are includible in the income of the member or patron when paid or allocated.	1. The Secretary of the Treasury or his delegate (after consultation with the Secretary of Agriculture) could be granted authority to prescribe such regulations as may be necessary to carry out the purposes of this Act. These regulations would provide that: a. Income from marketing commodities received under a 1983 PIK program is treated as patronage source income deductible to the cooperative (this rule would also protect the exemption of exempt farmers' cooperatives), regardless of whether the cooperative receives the commodity from the taxpayer or from the Commodity Credit Corporation on behalf of the taxpayer.

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13. Installment Payment of Estate Tax	Estate tax attributable to the value of an interest in a closely held business can be deferred and paid over up to 14 years if certain requirements are satisfied. Only interests in active businesses, as opposed to passive investments, are eligible for the installment payment provision.	b. Amounts received directly by a cooperative under the 1983 PIK program (e.g., rice and cotton cooperatives) would be treated as received on behalf of the member or patron signing the PIK contract. Real property withdrawn from production in exchange for a payment-in-kind under a 1983 PIK Program would be treated as used in the active conduct of farming. An anti-speculation rule would limit the estate tax provisions to property owned on February 23, 1983, or to property inherited or acquired by gift from an individual who owned it on February 23, 1983.
14. Definition of 1983 PIK Program		For purposes of the proposed alternative, crops that would have been planted before December 31, 1983, will be treated as a 1983 crop.

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15. Require study on who getting what		The Treasury Department (in consultation with USDA) would be required to submit a study on the effects of the PIK program and the proposed alternative.